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January 20, 1995

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W. - Room 222
Washington, D.C. 20554

JAN 20 1995

RE: Ex Parte Notice
CC Docket No. 94-1

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Dear Mr. Caton:

MCI made several ex parte presentations in this docket concerning "Operating Cash Flow." These ex partes contained several misstatements and mischaracterizations. USTA is filing the attached information to set the record straight.

The original and a copy of this ex parte notice are being filed in the Office of the Secretary. Please include it in the public record of this proceeding.

Respectfully submitted,

Mary McDermott

Mary McDermott
Vice President & General Counsel

cc: R. Metzger
M. Katz
P. Belvin
K. Brinkman
J. Casserly
[redacted]

THE UNITED STATES TELEPHONE ASSOCIATION RESPONSE TO MCI EBITDA PRESENTATION

A. Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA)

MCI uses a comparison of EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization) ratios between the local exchange industry and other industries to conclude that RBOC/LEC earnings are excessive. But EBITDA is not a measure of profitability. It measures earnings before subtracting out a number of significant operating expenses, most notably depreciation and amortization expenses.

EBITDA ratios can be used ***ONLY*** *to compare firms* ***WITHIN A SINGLE INDUSTRY.*** *EBITDA is not a primary analysis tool for financial analysts.*[1]

B. EBITDA Within the LEC Industry

An industry that is capital intensive, such as the LEC industry, will have a higher proportion of depreciation and amortization as a share of total operating costs, and relatively higher interest expenses. Consequently, the industry will have higher EBITDA ratios.

Comparisons of EBITDA ratios between industries are misleading. EBITDA ratios differ between industries because of the very nature of the different product markets and production processes for each industry.

Because of the fundamental nature of their business, LECs are more capital intensive than the IXCs. It takes more capital for a LEC to produce a given amount of sales revenue:

1993 DATA	*RBOCS*	*AT&T*	*MCI*
Net Property, Plant and Equip. as a Percent of Total Assets	*83%*	*32%*	*65%*
Sales as a Percent of Net Property, Plant and Equip.	*60%*	*345%*	*154%*

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1. Financial analysts who have examined EBITDA as a measure of cash flows (to determine a measure of business risk) are careful not to use the raw EBITDA data. For example, Duff & Phelps, in a recent report calculate the coefficient of variation of EBITDA before attempting any comparisons across industries because without doing so, it "... is not comparable between industries with absolute levels of EBITDA or interest coverage." Duff & Phelps, "Competitive Risk Analysis: Telecommunications as Industriales: Telecommunications Firms' Financial Performance continues to Approach the Level of Industriales", October, 1994, Appendix A.

C. Dividend Payout Ratios of Wholly-Owned Subsidiaries

In its ex parte, MCI compared the dividend payout ratios of the Bell Operating Companies to the average payout ratio of publicly held U.S. corporations. This comparison is invalid. The BOCs are wholly owned subsidiaries of Regional Holding Companies. The normal financial guidelines followed by a publicly held corporation in setting dividend payout ratios do not apply to wholly-owned subsidiaries that do not have external shareholders. Like many other U.S. subsidiary/parent corporate combinations, some of these subsidiary BOCs pay out 100% of their income to their parent corporation.

D. Return-On-Equity Comparison

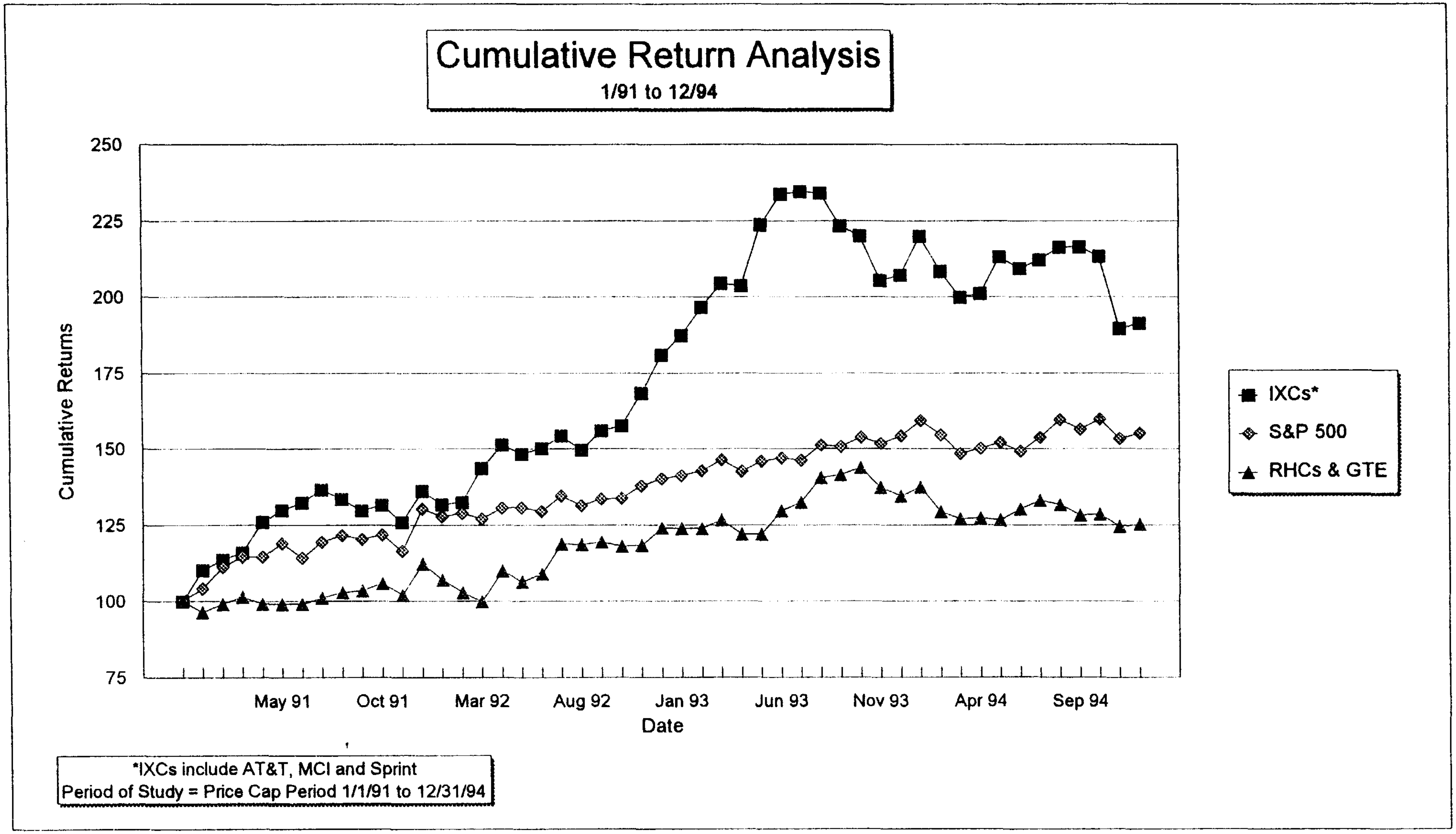
MCI presented return-on-equity data that USTA has been unable to replicate. It is clear, however, that MCI used Regional Holding Company data when it should have used Bell Operating Company data.

USTA sets out below the comparison of returns on equity that it has previously presented in this docket. These return figures are properly adjusted for extraordinary items (such as SFAS 106).

1993 DATA	*RBOCS*	*AT&T*	*MCI*
Return on Equity	*9.28%*	*19.61%*	*15.86%*

E. Cumulative Returns

In its ex parte, MCI included a chart that compared cumulative returns. Attached is the same information, except that the initial point on the chart is the time the price cap plan was implemented. As is clear from the attached chart (and data previously presented by USTA and the price cap LECs), LEC returns have consistently been less then the IXC's and the S&P 400.



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